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Message Text

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ACTION EUR-12

INFO OCT-01 ISO-00 AID-05 CEA-01 CIAE-00 COME-00 EB-08
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R 102126Z NOV 77
FM AMEMBASSY PARIS
TO SECSTATE WASHDC 1591
INFO AMEMBASSY VIENNA

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TAGS: OECD, ECON
SUBJECT: ECONOMIC AND DEVELOPMENT REVIEW COMMITTEE
(EDRC) -- REVIEW OF AUSTRIA

REF: EDRC(77)26, PARIS 32416

1. SUMMARY: EDRC DEBATED THE HARD SCHILLING POLICY AT LENGTH AFTER AGREEMENT WAS REACHED ON THE SECRETARIAT'S FORECAST FOR 1978. THE AUSTRIAN DELEGATION (HEADED BY GEHR OF THE FEDERAL CHANCELLERY) CONVINCED THE COMMITTEE OF THE UNALTERABLE ATTACHMENT OF THE GOA TO THE CURRENT HARD CURRENCY POLICY, AND IT WAS SUBSEQUENTLY CONCLUDED THAT THE DRAFT SURVEY WOULD BE REVISED TO ACCEPT THIS POLICY AS GIVEN AND FOCUS ON THE IMPLICATIONS FOLLOWING FROM IT. THE AUSTRIAN DEL ANNOUNCED THAT MAINTENANCE OF THE HARD SCHILLING POLICY WAS REQUIRED BY THE LABOR UNIONS FOR THEIR SUPPORT OF THE 1978 AUSTERITY PROGRAM. END SUMMARY

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2. OUTLOOK FOR 1978: THE SECRETARIAT AND THE AUSTRIAN DELEGATION WERE IN BASIC AGREEMENT WITH THE SECRETARIAT'S FORECAST FOR 1978 WITH NEGLIGIBLE EXCEPTIONS. WITH REGARD TO THE IMPACT OF RECENT POLICY MEASURES THE AUSTRIAN DELEGATION SAID THAT THESE MEASURES SHOULD BE SEEN IN A MEDIUM-TERM CONTEXT DESIGNED TO ARREST THE CURRENT UNFAVORABLE TRENDS

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AND THUS SET THE STAGE FOR LONGER-TERM ADJUSTMENTS.
THEY ARE NOT INTENDED AS SHORT-TERM MEASURES TO
QUICKLY REMEDY CURRENT DIFFICULTIES.

3. EXCHANGE RATE POLICY: JUSTIFICATION OF AUSTRIA'S
HARD CURRENCY POLICY AND THE SECRETARIAT RECOMMENDATIONS
REGARDING THAT POLICY WERE THE PRINCIPAL POINTS OF
DISCUSSION THROUGHOUT THE DAY-LONG REVIEW OF AUSTRIA.
THE SECRETARIAT AND SEVERAL DELEGATIONS NOTED A) THE
DECLINING COMPETITIVE POSITION OF AUSTRIAN INDUSTRY,
PARTICULARLY WITH REGARD TO IMPORT PENETRATION BY
FOREIGN PRODUCERS, AS WELL AS INCREASING RELATIVE
PRICES IN THE AUSTRIAN TOURIST SECTOR AND B) INVESTMENT
SHIFTS AWAY FROM THE EXPOSED SECTOR AS PARTICULARLY
TROUBLESOME ASPECTS OF THE RECENT AUSTRIAN EXPERIENCE.
THE SWISS DELEGATE PROPOSED THAT A HARD CURRENCY
POLICY REQUIRES A STEADY IMPROVEMENT IN PRODUCTIVITY,
PARTICULARLY THROUGH SHIFTS TO ADVANCED SOPHISTICATED
INDUSTRY, SUCH SHIFTS USUALLY REQUIRING HIGH LEVELS OF
INVESTMENT AND PRECEDENT HIGH PROFIT RATES, CONDITIONS
NOT PRESENT IN AUSTRIA.

4. THE AUSTRIAN DELEGATION DID NOT SHARE THE
SECRETARIAT'S ANALYSIS OF ITS DETERIORATING
COMPETITIVE POSITION AND CITED SPECIFICALLY QUESTIONS OF
STRUCTURE IN INDUSTRY AND TOURISM AS THE BASIC CAUSE
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OF THE RECENT IMPORT/EXPORT PERFORMANCE; USING
THE RESULTS OF CERTAIN ECONOMETRIC MODELS TO SUPPORT
THEIR ARGUMENT. THE AUSTRIAN DELEGATION BELIEVED THAT
PSYCHOLOGICAL FACTORS AND THE DISCIPLING EFFECT OF AN
APPRECIATING CURRENCY ON PRICES WERE THE PRINCIPAL
ARGUMENTS IN FAVOR OF MAINTAINING THE HARD CURRENCY
OPTION. IN ADDITION, THE HEAD OF THE AUSTRIAN DEL
ANNOUNCED TO THE COMMITTEE THAT AUSTRIAN LABOR UNIONS
HAD RECENTLY GRANTED THEIR SUPPORT TO THE 1978 AUSTERITY
PACKAGE WITH THE CAVEAT THAT THE HARD CURRENCY OPTION
BE UPHELD. ON THE PROBLEM OF COMBATTING SPECULATIVE
PRESSURES, THE REPRESENTATIVE OF THE AUSTRIAN
NATIONAL BANK PROPOSED THAT IN THE FIRST CASE, RUMORS
OF A MORE FLEXIBLE EXCHANGE POLICY (IN AN OBVIOUS
REFERENCE TO THE SECRETARIAT'S RECOMMENDATIONS) MUST BE
AVOIDED AND AS A LAST RESORT AND ONLY IF NECESSARY,
CAPITAL RESTRICTIONS MIGHT BE CONSIDERED.

4. UNEMPLOYMENT: THE AUSTRIAN DEL ADMITTED THAT THE
CURRENT AUSTERITY PROGRAM INVOLVED A RISK OF HIGHER
RATES OF UNEMPLOYMENT CONCEDING THAT UNEMPLOYMENT OF THE
DOMESTIC LABOR FORCE COULD REACH 3 PERCENT BY THE END

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OF 1978. HE ADDED THAT THE LABOR UNIONS WERE FULLY

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AWARE OF THIS RISK, BUT THEY AGREED TO ACCEPT IT IN ORDER TO MAINTAIN THE HARD CURRENCY OPTION AND ITS PRICE DISCIPLINE. NOTING THAT THE RECENT STRENGTH OF THE LABOR MARKET IN AUSTRIA WAS DUE IN SHIFTS OF EMPLOYMENT TO THE TERTIARY SECTOR (AND NOT EXCLUSIVELY LABOR HOARDING), THE AUSTRIAN DEL SUGGESTED THAT UNIONS WOULD HAVE TO BE CONVINCED THAT SUCH SHIFTS RESULTED IN LOWER RATES OF PRODUCTIVITY GROWTH AND WOULD, THEREFORE, HAVE TO MODERATE THEIR DEMANDS FOR REAL WAGE INCREASES. IN THIS REGARD, THE HEAD OF THE AUSTRIAN DEL, DURING HIS INTRODUCTORY STATEMENT, ARGUED THAT THE CURRENT AUSTRIAN BOP DIFFICULTIES CAN BE TRACED ALMOST EXCLUSIVELY TO EXCESSIVE NOMINAL WAGE INCREASES TO 1975, BUT THAT THE EFFECTIVE FUNCTIONING OF THE AUSTRIAN'S INCOMES POLICY IS SLOWLY CORRECTING THIS MISTAKE.

5. INVESTMENT: IN CITING STRUCTURAL PROBLEMS AS THE SOURCE OF AUSTRIA'S BALANCE OF PAYMENTS DIFFICULTIES, THE AUSTRIAN DELEGATION AGREED THAT CORRECTION OF THE STRUCTURAL DIFFICULTIES WOULD REQUIRE UNUSUALLY HIGH
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RATES OF INVESTMENT EVEN BY HISTORICAL LEVELS. NEW POLICIES WERE REPORTED TO BE UNDER CONSIDERATION TO SUBSIDIZE INTEREST CHARGES AND TO OFFER PROJECT SPECIFIC INCENTIVES WHICH MIGHT BE MORE EFFICIENT THAN TAX INCENTIVES IN ELICITING AND DIRECTING THE NECESSARY INVESTMENT.

6. POLICY CONCLUSIONS: THE AUSTRIAN DELEGATION ADAMANTLY AND PERSISTENTLY REFUSED TO AGREE WITH THE IMPLICATIONS IN THE SECRETARIAT REPORT THAT THE HARD CURRENCY OPTION BE MADE MORE FLEXIBLE. A COMPROMISE WAS EVENTUALLY REACHED UNDER WHICH THE SECRETARIAT WOULD PRESENT THE HARD CURRENCY OPTION AS GIVEN, BUT WOULD PRESENT THE IMPLICATIONS OF THAT CHOICE AS CONSTRAINTS ON OTHER POLICY DECISIONS. SPECIFICALLY, IT WAS AGREED THAT THE DIFFERENTIAL GROWTH OF DEMAND IN AUSTRIA AND ITS MAJOR TRADING PARTNERS WAS THE ROOT CAUSE OF THE BALANCE OF PAYMENTS DIFFICULTY AND THEREFORE THAT A CONTRACTION OF AUSTRIAN DEMAND WOULD BE NECESSARY UNLESS FOREIGN DEMAND SURGED (AN UNLIKELY PROSPECT) OR THE SCHILLING WERE MORE FLEXIBLE. IT WAS AGREED THAT THE AUSTRIAN ECONOMY NEEDED A SHORT-TERM SLOWDOWN OF DEMAND GROWTH TO ARREST DETERIORATING TRENDS, BUT THAT POLICY INSTRUMENTS WOULD HAVE TO BE DESIGNED TO ELICIT EXPENDITURE AND INVESTMENT SWITCHING THUS AMELIORATING THE STRUCTURAL PROBLEMS. THE AUSTRIAN DELEGATION DID NOT OUTLINE THE DETAILS OF THE POLICY PLANNED IN THIS REGARD. THE AUSTRIAN DELEGATION ON SEVERAL OCCASIONS EMPHASIZED THE NEED FOR STRONGER EXTERNAL STIMULUS TO PERMIT THE CONTINUATION OF FULL EMPLOYMENT POLICIES IN AUSTRIA, ARGUING THAT A SMALL EXPORT-ORIENTED COUNTRY SUCH AS AUSTRIA COULD NOT PURSUE A FULL EMPLOYMENT POLICY ALONE.
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